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SUBJECT: SERBIA'S PENDING PUBLIC SECTOR REFORM NOT ENOUGH

Summary

11. (SBU) Serbia is moving forward in cutting its bloated state bureaucracy in an effort to pacify the IMF's calls for Serbia to shrink its budget deficit. In its first step, the Serbian Government adopted a draft law that cuts state administration by 10% and sent it to the Parliament with the promise that this is just the beginning of serious public sector reform. Independent trade unions and analysts accused the Government of hastily doing such a complex task only to please the IMF, without any real consideration of the impact. Officials in the Finance Ministry told us the action would have a minimal impact on budget costs since it excluded core spending in education, health, and security institutions. Experts claim this would be a small - and easy - step in the right direction, but the desperately needed public sector reform had to be much broader. End summary.

Law on Reducing State Employees Sent to Parliament

12. (U) On October 9, the government agreed to send a draft Law on Establishing the Maximum Number of Employees in Administration to the Parliament for adoption. This was the first step in public sector reform, Prime Minister Cvetkovic told the press after the government session. Cvetkovic said the law would cut administration by 10%, or by 3,400 employees, by January 1, 2010. The cut would include all agencies and ministries except Interior, Defense, the State Security Agency (BIA), and prison administration (part of the Justice Ministry). The proposed law would also restrict the total number of full time employees working for the state administration to 28,400, and the number of part-time employees to 2,840 (10% of the number of permanent employees). Parliament plans to debate the law by the end of October.

13. (SBU) In addition to this draft law, on October 22 Government forwarded to the Parliament the draft Law on Establishing the Maximum Number of Employees in Local Administration limiting it to four employees per 1,000 citizens, what would result in 5,468 job cuts. Several local mayors told us on October 19 that the government had done little to consult with them on these potential local cuts. In addition, Cvetkovic said that separate from the central and local administration cuts, the Government had adopted plans to lay-off 2,500 persons from the judicial system.

The State Keeps Growing and Growing

14. (U) Local press reported that since the end of the Milosevic era, Serbia's central administration has grown from 8,100 employees in 2000 to over 30,000 in 2009. Currently there are an estimated 34,000 workers supporting the administrative work of the government ministries. Essentially these are policy people and support staff based primarily in Belgrade. While some of this growth was due to unchecked political patronage, a significant portion of the growth is

because the Serbian state apparatus assumed many functions from the former federal administration (around 12,000 employees) after the dissolution of At that time, Serbia assumed responsibility for the Ministries of Foreign Affairs and Defense, as well as various offices, such as the Weather Service.

15. (U) Serbia's public sector (i.e. state administration, local governments and public companies) employs roughly one quarter (619,000) of the 2.6 million persons currently working in Serbia, World Bank Country Economist Lazar Sestovic told us on October 20. Out of this number, the Central Government employs 34,000 in central administration. Local self-government (municipalities) have 38,000 employees paid from their local budgets. The police, military and security agencies employ around 90,000 people. Education and health services have around 130,000 employees each. Public companies, including local utilities and state companies such as JAT Airways, Serbian Railways, Serbian Electric Power(EPs), Telekom, and Srbijagas have over 170,000 people on their payrolls.

Objective Standards, But No Savings until 2011

16. (U) Staff cuts would be determined by the "necessity of the position" and the "professional and unbiased evaluation" of each employee, Deputy Prime Minister Mladjen Dinkic told the press on October 9. To compensate for the hit, laid-off workers would receive severance packages, while employees with less than five years until retirement would not be cut. Both PM Cvetkovic and DPM Dinkic avoided stating the actual savings for the upcoming 2010 budget and would not speculate as to whether the cut would be enough to satisfy

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the IMF's request for Serbia to cut its projected 2010 budget deficit by 0.5% of GDP to 3.5%. Instead, Cvetkovic and Dinkic explained that the real savings would be visible beginning in 2011 and that the job cuts would bring more indirect savings by simplifying procedures for citizens and businesses by reducing bureaucracy. Cvetkovic said he hoped that Serbia would gain more credibility with the IMF once it showed it was serious about reform.

Resistance By Ministers: No Cuts In My Ministry

17. (SBU) The government's draft law will likely face strong debate in the Parliament. Opposition Democratic Party of Serbia (DSS) has already called for the Parliament to oversee the cuts, while several members of the ruling coalition have criticized the draft law as well. Infrastructure Minister Milutin Mrkonjic, from the Socialist Party of Serbia (SPS), stated on September 18 that he was against the cuts and that he would vote against them at the government session. "I have 190 employees in my Ministry, they all work and I am happy with them. The Serbian government's duty is to hire all of its citizens, and I don't see what we get by firing people," Mrkonjic said. Dragan Markovic Palma, leader of United Serbia party, said on September 28 that he was against cuts in any department and that the government should look for possibilities to create new jobs instead. However, Palma said he would respect the decision if the law was adopted. Even Milan Markovic, Minister of State Administration and Local Self-Government and member of the Democratic Party (DS), stated in an interview to daily Politika on September 16 that he would not cut staff in his ministry since it did not have any excess labor. Rather than cutting staff, many in government have submitted requests to expand the size of ministries. The head of the Finance Ministry's budget preparation department Svetlana Anokic told us that she had received requests for 8,800 new jobs in state administration.

State Secretary, Budget Office Head: Not Enough

18. (SBU) Finance Ministry State Secretary Vuk Djokovic told us unofficially on October 14 that this law touches "only the tip of the iceberg" and does not go deep into reforms. "We are not touching education, health, defense, police, where the big numbers are. This is just a cosmetic change done at the wrong time, at a moment when we need to work on accession to the EU which is a huge task for the administration," Djokovic said. Anokic told us on October 15 that

the actual savings that this cut would bring to the 2010 budget was minimal, due to the need to pay severance packages. As a result, the government would save in 2010 just \$14.3 million compared to an expected deficit of \$1.7 billion. She claimed this would be insufficient to satisfy the IMF's demand to cut the projected 2010 deficit to 3.5% of GDP, or \$215 million.

Trade Union Nezavisnost: Against Draft Law

¶9. (U) Trade unions are typically divided on the proposed law: while the largest trade union (SSSS) supported the draft law, the second largest trade union Nezavisnost (Independence) rejected the draft and accused SSSS of always nodding yes to the government. At an October 15 round table, Nezavisnost leader Branislav Canak stated that the draft law was "very frivolous, irresponsible, hasty and not statesmanlike" and in direct opposition to Serbia's labor law and parts of the General Collective Agreement. Instead of taking a few years for such an important strategic reform, the Government was doing this quickly on the eve of the IMF visit, Canak said. He speculated that the IMF would not swallow this and would only give its support to Serbia under unfavorable terms. Canak said that party membership would be the key criteria for keeping positions. This would leave the administration full of incapable employees who had jobs only because of their party membership, said Canak.

¶10. (U) Justice and police trade union leaders complained at the round table they were not even invited to the dialogue with the government, and claimed this was not a good time to reform the state when Serbia's unemployment rate was already more than 16%. However, all union representatives at the round table agreed that public sector was too large for the size of Serbia's economy and that eventual rationalization was necessary. The unions, however, said they were responsible to employees and claimed there were other ways to save budget funds such as addressing corruption and the gray economy.

Experts: Reform Must Be Much Broader

¶11. (SBU) Miladin Kovacevic of the Economic Institute think-tank

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told us on October 16 that this law was just "one small step in the right direction." Kovacevic said cutting state administration was one small part of three goals for wider reform: reducing public consumption; increasing public sector efficiency; and establishing sustainable social functions of the state with regard to pension and health funds. Kovacevic explained that for Serbia, public sector reform was a must and that Serbia had hit the wall since the current growth model based on the inflow of foreign funds, previously fueled by privatizations and FDI, had been exhausted. If Serbia does not reform its public sector it will "continue to face an economic crisis, including debt crisis as soon as next year. Serbia will remain a poor country of poor citizens and pensioners," Kovacevic said.

COMMENT

¶12. (SBU) While Serbia's first attempt at public sector reform is laudable, real reform needs to be much deeper and broader. Serbia cannot expect to claw its way out of the economic crisis solely by trimming the margins of its budget. Only with comprehensive reform that seeks to reduce the public sector's role in the overall economy can Serbia reposition itself for a post-crisis economy. To do that will require greater political will and a firm stance by the IMF during upcoming negotiations. End Comment.
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